

Untitled
COMMONWEALTH OF MASSACHUSETTS
BEFORE THE
DEPARTMENT OF TELECOMMUNICATIONS AND ENERGY

D. T. E. 00-68

JOINT PETITION OF
WESTERN MASSACHUSETTS ELECTRIC COMPANY
NEW ENGLAND POWER COMPANY
AND
FITCHBURG GAS AND ELECTRIC LIGHT COMPANY

FOR APPROVAL OF ASSET DIVESTITURE

DIRECT TESTIMONY OF

RICHARD A. SODERMAN
AND
RICHARD M. KACICHON

Untitled

SEPTEMBER 8, 2000

TABLE OF CONTENTS

I. INTRODUCTION 1

II. DIVESTITURE OBJECTIVES 3

IV. AUCTION RESULTS 6

IV. EXEMPT WHOLESALE GENERATOR STATUS 15

I. INTRODUCTION

Q. Mr. Soderman, please state your full name, your business address, and your position with Western Massachusetts Electric Company ("WMECO" or the "Company").

A. My name is Richard A. Soderman. My business address is 107 Selden Street, Berlin, Connecticut 06037. I am Director of Regulatory Policy and Planning for Northeast Utilities Service Company ("NUSCO") which provides centralized services to the operating companies of the Northeast Utilities ("NU") system,

Untitled

including WMECO.

Q. In your position, what are your responsibilities?

A. As Director of Regulatory Policy and Planning, I am responsible for developing and implementing regulatory policies and practices for the NU system companies. As part of these responsibilities, I have directed the preparation and filing of various plans and proposals related to electric industry restructuring, including those necessary to implement the Massachusetts Electric Industry Restructuring Act (the "Act").

Q. Mr. Kacich, please state your full name, your business address, and your position.

A. My name is Richard M. Kacich. My business address is Millstone Nuclear Power Station ("Millstone"), Rope Ferry Road - Route 156, Waterford, Connecticut 06385. I am Director of Business Services for Northeast Nuclear Energy Company ("NNECO"), a wholly owned subsidiary of NU, which operates the Millstone Station on behalf of WMECO and the other owners.

Q. In your position, what are your responsibilities?

A. As Director of Business Services, I am responsible for a wide range of activities associated with Millstone and the NU companies. I report to the Millstone Chief Nuclear Officer. During the recent auction of Millstone, I was responsible for

Untitled

the administration of the auction project at the site and for acting as a primary interface with the auction agent J.P. Morgan Securities, Inc. ("J.P. Morgan"). Regarding the sale and transfer of the station to new ownership, I am sharing with a representative of Dominion Resources, Inc. ("Dominion") the leadership of the integration team, which is responsible for effecting a smooth transition of Millstone to the new owner.

Q. Mr. Soderman, have you ever testified before the Department of Telecommunications and Energy?

A. Yes. I have testified before the Department of Telecommunications and Energy (the "Department") on numerous occasions, most recently in WMECO's restructuring plan proceeding, D.T.E. 97-120, and WMECO's securitization proceeding, D.T.E. 00-40.

Q. Mr. Kacich, have you testified before the Department?

A. Yes, I testified in WMECO's restructuring plan proceeding, D.T.E. 97-120.

Q. What is the purpose of your joint testimony?

A. The purpose of our testimony is to support WMECO's, New England Power Company's ("NEP") and Fitchburg Gas and Electric Light Company's ("FG&E") (collectively, the "Petitioners") joint petition to the Department for approval of the sale of Millstone

Untitled

to Dominion Nuclear Connecticut, Inc. ("DNC"), and related findings and approvals. DNC is an indirect, wholly-owned special-purpose subsidiary of Dominion Energy, Inc., which in turn is a wholly-owned subsidiary of Dominion. Dominion is the successful bidder for Millstone and intends to assign its rights to acquire Millstone to DNC. We provide support for the conclusion that the sale meets applicable statutory requirements and Department standards, and is consistent with each of the Petitioners' Restructuring Plans (or Restructuring Plan Settlements) (see D.T.E. 97-120 (WMECO), D.P.U. 96-25 (NEP) and D.T.E. 97-115 (FG&E)). Finally, we provide support for the request for findings that the divested Assets are "eligible facilities" under Section 32 of the Public Utility Holding Company Act of 1935 ("PUHCA"), which findings are essential to the designation of the buyer as an Exempt Wholesale Generator ("EWG").

II. GOVERNING AUTHORITY

Q. Please describe your understanding of the legislative and regulatory environment within which the divestiture of Millstone is occurring.

A. On November 25, 1997, the Massachusetts Legislature enacted Chapter 164 of the Acts of 1997 (Massachusetts Electric Utility Restructuring Act) (now codified, in pertinent part, in G.L. c. 164) (the "Restructuring Act"). The Restructuring Act, among other directives, mandated the divestiture of non-nuclear

Untitled

generating assets by electric utility companies. Although the divestiture of nuclear assets was not required by the Act, the sale of these assets is consistent with the Act's directive that "[t]he interests of consumers can best be served by an expedient and orderly transition from regulation to competition in the generation sector consisting of the...functional separation of generation services from transmission and distribution services." Restructuring Act, Section 1(m). It is also consistent with the disaggregation of vertically-integrated electric utilities through the sale of generation assets to competitive suppliers, a long-standing goal of the Department (see D.P.U. 96-100 (December 30, 1997)).

Further, divestiture of the Millstone nuclear units is entirely consistent with the requirement in the Restructuring Act that electric utility companies mitigate stranded investments. Under the Restructuring Act, mitigation includes sale of all generating facilities (see G.L. c. 164, § 1) and any electric company wishing to recover transition costs is required to mitigate (see G.L. c. 164, §1G(d)(1)). Accordingly, the sale of the Millstone nuclear units is consistent with the divestiture of generating assets to competitive entities and furthers the policy goals of the Commonwealth.

Q. Is there governing authority for the sale of nuclear generating assets?

A. Yes. The Joint Petition for Approval of Asset Divestiture

Untitled

submitted today in this proceeding sets forth the governing authority. In sum, the Department has general supervisory authority of all gas and electric companies under several sections of Chapter 164 of the General Laws. In addition, the Department has previously ruled on sales of nuclear generation. See, e.g., Boston Edison Company and Commonwealth Electric Company, D.T.E. 98-119/D.T.E. 98-126, p. 5 (March 22, 1999) ("sale process is equitable and maximizes the value of the existing generation facilities being sold").

Q. Does the sale of Millstone meet the applicable tests?

A. Yes. Millstone was offered in a public auction conducted pursuant to Connecticut General Act 98-28, "An Act Concerning Electric Restructuring". The Connecticut Department of Public Utility Control ("CT DPUC") selected J.P. Morgan, a nationally prominent investment banking firm, to conduct the auction under the supervision of the CT DPUC's Utility Operations Management Analysis ("UOMA") auction team. The sale process ensured complete, uninhibited and non-discriminatory access to all data and information and was equitable and maximized the value of the assets being sold. Paul M. Dabbar, of J. P. Morgan, explains in detail the auction process in his pre-filed direct testimony (Attachment 2 to this filing).

Q. Did any affiliate of Northeast Utilities or Consolidated Edison Company, Inc. (with whom NU has entered into an Agreement and Plan of Merger) participate in this auction?

Untitled

A. No.

Q. Did NU institute and strictly comply with a Nuclear Auction Protocol?

A. Yes. NU put in place a Nuclear Auction Protocol to make sure that employees were aware of their confidentiality requirements and other responsibilities as a part of the auction process. In addition, J.P. Morgan strictly controlled the flow of information on a need-to-know basis.

Q. Who chose the winning bidder?

A. J. P. Morgan and UOMA determined the winning bidder. The role of NU and NNECO in the auction process was thus limited to managing the Auction Center, managing the auction website, conducting the orientation presentation, providing tour guides for site visits, providing data to J.P. Morgan as requested, and responding to bidder questions under the supervision of J.P. Morgan.

Q. In your opinion does the sale of the Millstone assets comply fully with all statutory and/or regulatory requirements pertinent to the sale of these assets?

A. Yes.

III. AUCTION RESULTS

Q. Please describe the outcome of the auction process.

A. The successful completion of the sale of Millstone was announced on August 7, 2000 by J.P. Morgan. The winning bidder is Dominion. Dominion is the largest fully-integrated natural gas and electric power provider in the United States with over \$24 billion in assets, over \$8 billion in annual revenue, and over \$2 billion in annual operating cash flow. Virginia Power, which is the licensed owner and operator of the North Anna and Surry nuclear stations, is also a subsidiary of Dominion and has one of the finest records of safe nuclear plant operation in the world, having, for example, achieved top rankings for its North Anna and Surry plants since 1991 from both the Institute for Nuclear Power Operations and the Nuclear Regulatory Commission (the "NRC"), while maintaining an average capacity factor in excess of 90 percent over the last five years. Thus, the Dominion companies possess substantial nuclear experience and capabilities that are sufficient to ensure that the Millstone units can and will be operated safely and reliably.

Q. Please characterize the winning bid.

A. The winning bid is a significant sum and is further evidence that the auction was equitable and maximized the value of the assets being sold. The sale price was \$1.298 billion, subject to certain adjustments at closing.

Untitled

Q. What exactly is being sold?

A. On August 7, 2000, the Petitioners and Dominion entered into a purchase and sale agreement (the "PSA") for the sale of Millstone. In addition to interests covered by the PSA, on August 7, 2000 the Connecticut Municipal Electric Energy Cooperation ("CMEEC") executed a separate purchase and sale agreement with Dominion, which binds CMEEC to the terms of the PSA. These two agreements provide for the sale of 100 percent of Millstone Units 1 and 2 and 93.47 percent of Millstone Unit 3. (The Massachusetts Municipal Wholesale Electric Company and Central Vermont Public Service Company chose not to sell their ownership shares in Millstone Unit 3, which are 4.80 percent and 1.73 percent, respectively.) In addition, NNECO assets, as well as inventory and fuel assets associated with Millstone Units 2 and 3, will also be sold.

Q. Are there any decommissioning or Purchased Power Agreement ("PPA") requirements as part of this sale?

A. A significant added benefit is that except in limited circumstances noted below the sale requires no decommissioning top-off payments, nor is a PPA part of the PSA. Consequently, except as noted, the sale proceeds are not diminished by requirements for the sellers to add additional moneys to the existing Millstone Units 1, 2 or 3 decommissioning funds at closing or for the long-term purchase of power at a price that

Untitled

in other sales have been at above-market prices, resulting in a net cost to customers. The details of the decommissioning top-off payment are discussed later in this testimony.

Q. Where are the terms of the sale contained?

A. The PSA is the principal document setting forth the terms under which the Joint Petitioners and the other co-owners will sell the assets to DNC. The PSA is appended as Attachment 5 to this filing. Certain other agreements (the "Related Agreements") identified as exhibits in the PSA, including an Interconnection Agreement required to satisfy NRC criteria for off-site power for the new buyer, which sets forth the provisions of the ongoing relationships of the seller(s) and buyer, are being filed with the PSA.

Q. Please summarize the key terms of the sale as set forth in the PSA.

A. The sale price for elements of the Millstone assets is as follows:

Unit 1 Facilities \$1,000,000

Unit 2 Facilities \$401,500,000

Unit 3 Facilities \$790,518,600

Untitled

Unit 1 Nuclear Fuel \$0

Unit 2 Nuclear Fuel \$41,900,000

Unit 3 Nuclear Fuel \$62,800,000

TOTAL \$1,297,718,600

The sale of Millstone includes, without limitation: the electric generation equipment and related facilities; the assets of NNECO; the real estate on which the electric generation equipment and related facilities are located and related rights; the assets comprising the decommissioning funds, including all income, interest and earnings accrued thereon, together with all related tax accounting, decommissioning studies and cost estimates, and all other books and records related thereto; agreements and permits associated with the plants; plant books and records; and emission credits and allowances. Excluded from the sale are most transmission, distribution and substation facilities (and associated real estate rights), cash, notes, and receivables, and any claims of the Petitioners (in connection with Pre-1983 Spent Nuclear Fuel) related or pertaining to the Department of Energy's ("DOE") defaults under the DOE Standard Contracts accrued as of the Initial Closing Date (as defined in the PSA).

Dominion also agreed to acquire and assume the existing agreements for the sale of capacity and energy from Millstone

Untitled

Units 2 and 3; these agreements were provided to the Department on November 16, 1999. DNC will continue to sell WMECO's former share of the output of Millstone Units 2 and 3 from closing until December 31, 2001, pursuant to the terms of those agreements.

Q. Is the purchase price for Millstone subject to adjustment?

A. The purchase price is subject to adjustment to account for, among other things, certain expenditures incurred during the period between the date of signing of the PSA and the date of closing and for inventories of fuel and certain materials and supplies on hand at the closing. In addition to standard commercial terms, such as indemnity provisions and representations and warranties, there are a number of conditions to the closing of the sale, which include: the receipt of all regulatory approvals; execution of all of the related agreements; and the absence of any change in or effect on Millstone which would constitute a "Material Adverse Effect", as defined in the PSA. The PSA provides for the closing to occur within 15 days of the satisfaction of the closing conditions. The parties have agreed to cooperate with each other and use commercially reasonable efforts to obtain the necessary regulatory approvals in order to have a single, coordinated closing on or about April 1, 2001. The PSA may be terminated by either party thereto if all conditions to closing have not been met by April 22, 2001, although under certain circumstances that date can be extended.

Untitled

Q. How will Millstone Station be operated and maintained prior to closing?

A. NNECO is obligated to operate and maintain Millstone in accordance with Good Utility Practice until the closing.

Q. Please describe the potential for a decommissioning top-off payment.

A. Although a "top-off" payment per se is not a condition of the sale, there are certain limited circumstances where the selling owners, including WMECO, might be required to make further contributions to the decommissioning funds transferred to DNC.

The first of these circumstances might arise if earnings on the current trust amounts are lower than anticipated in the period between the execution of the PSA and the actual closing of the sale. If that were to occur, the amounts in the decommissioning funds would be less than the amounts specified in the PSA and the separate agreement with CMEEC (\$268.3 million for Millstone Unit 1, \$252.9 million for Millstone Unit 2 and \$246.8 million for Millstone Unit 3). It is also possible that an earnings shortfall could result in a lower than specified level in the tax-qualified decommissioning funds, even if the overall amounts of the funds were as set forth in the PSA. In either event, WMECO and The Connecticut Light and Power Company ("CL&P"), on behalf of the sellers, are required to make sufficient

Untitled

contributions to the funds at closing to make them equal the amounts set forth in the PSA.

The second of these circumstances is dependent on the NRC's willingness to accept the parent guarantee of Dominion as a method of financial assurance for decommissioning expenses of Millstone Unit 1 pursuant to 10 C.F.R. § 50.75(e)(1)(iii). The license-transfer application submitted to the NRC has proposed this methodology, in accordance with NRC regulations. If this method is not accepted by the NRC, the Millstone Unit 1 decommissioning trust will need to be increased up to the minimum level required by the NRC for the Unit. The PSA requires DNC to fund 20% of the cost of this additional contribution, up to \$12 million. WMECO and CL&P, on behalf of the sellers, must contribute the balance of the required amount. As set forth in the NRC license-transfer application, absent NRC approval of the parent guarantee, it is estimated that approximately \$26 million will be required to bring the level of the Millstone Unit 1 decommissioning fund up to NRC requirements. Of this amount, WMECO and CL&P would be required to contribute approximately \$20.8 million.

The third circumstance could arise out of the requirement to transfer Millstone Unit 1 to DNC in a "cold and dark" condition. To the extent additional work remains to be done to achieve "cold and dark" status at the time of closing, WMECO and CL&P, on behalf of the sellers, must either reimburse the cost of such remaining work to DNC or add it to the Millstone Unit 1

decommissioning trust.

Finally, the PSA assumes closing will occur on April 1, 2001. If the closing is delayed past that date, the PSA provides that the decommissioning trust balance to be transferred to DNC will increase by 0.5% per month. Accordingly, if the closing occurs after April 1, 2001 certain sellers, including WMECO, may be required to make further contributions to the decommissioning trusts to fulfill this requirement.

Q. Please describe the obligations that DNC will be assuming when it purchases Millstone.

A. DNC will assume all liabilities related to Millstone, other than certain specifically enumerated "Excluded Liabilities." The liabilities that are to be assumed by DNC (as well as those Excluded Liabilities that are to be retained by the Petitioners) are set forth in detail in the PSA. Specifically noteworthy is DNC's assumption of all liabilities in respect to the decommissioning of the facilities following permanent cessation of operations, and the management, storage, transportation and disposal of spent nuclear fuel (including, without limitation, all fees payable to DOE under the DOE Standard Contracts accrued after the relevant closing date), except for any fees payable to DOE for Pre-1983 Spent Nuclear Fuel.

Q. Is DNC accepting environmental liability for the Assets?

Untitled

A. Yes. DNC will assume substantially all environmental liabilities related to the assets at closing. However, DNC does not assume liabilities associated with off-site disposal of hazardous wastes by the sellers prior to the closing, liabilities with respect to violations of environmental permits prior to the closing, criminal violations of environmental laws by the sellers prior to the closing, or certain other liabilities as more fully set forth in the PSA. Additionally, WMECO will also retain both pre- and post-closing environmental liabilities associated with use of exclusive easements it is reserving to itself for transmission and distribution operations and other purposes.

Q. Please describe the employee protections that are being provided by DNC to the Millstone employees under the PSA.

As described more fully in section 5.7 of the PSA, DNC will:

(1) Offer employment, for a period of at least twelve months from the Initial Closing Date to all employees of NU, WMECO or their affiliates who were employed in the operation of the Millstone plant at any time during the three-month period prior to the Initial Closing Date at levels of wages and overall compensation not lower than the lowest level of wages and overall compensation of each such employee in effect during the six-month period prior to August 7, 2000.

(2) Provide to any of the employees who accept the offer of

Untitled

employment and who are subsequently terminated without cause as a result of work force reduction or reorganization during the five year period immediately following the Initial Closing Date out-placement assistance in the form of workshops and tuition reimbursement of up to \$3,000 per employee for job related education or training.

(3) Provide severance benefits to any employee who accepts employment with Dominion and subsequently is terminated without cause as a result of work force reduction or reorganization during the five (5) year period immediately following the Initial Closing Date.

(4) Apply the period of each employee's prior service with WMECO or any of its Affiliates or any other service credited under the applicable employee benefit plans toward any eligibility, vesting or other waiting period requirements under the Dominion employee benefit plans.

(5) Allow the Millstone Station employees who, as of the Initial Closing Date, are 55 and older to retire on or after the Initial Closing Date and within twelve (12) months of the Initial Closing Date with full pension benefits if the sum of the employee's age and years of credited service (credited under the Plan as of the Initial Closing Date plus years of service with Dominion equals 85) at the employee's termination date.

(6) Establish and maintain for employees who accept employment

Untitled

with Dominion, employee benefit plans and programs generally comparable to the plans and programs provided to such employees by WMECO or its affiliates as of August 7, 2000.

Q. Are other regulatory approvals required prior to closing this sale?

A. As might be expected, the sale is contingent upon the approval of a number of regulatory agencies both at the federal and state level. As part of the sale process, to ensure that the buyer will comply with all applicable federal rules and regulations, NNECO and DNC have jointly submitted an application to transfer the NRC operating licenses for the plants. The parties will also submit all necessary applications to federal and state regulatory bodies. Once the sale is approved by the Department, and subject to the receipt of all other required regulatory approvals, the parties wish to close this transaction on or about April 1, 2001.

Q. Would you term the sale a success?

A. Yes. It was a success because it was fair and open and maximized the value of the divested assets. The fact that: (1) the sale price is one of the highest amounts received in a nuclear auction; (2) with limited exceptions, there is no required decommissioning fund top-off payment; (3) there is no power purchase agreement; (4) the winning bidder has a history of successful nuclear plant operations, and is highly regarded

Untitled

throughout the industry and by the NRC; and (5) future uncertainty regarding costs and liabilities associated with operation and decommissioning will no longer be borne by the Petitioners' customers, are irrefutable proofs of this success.

Q. Does the sale provide benefits to customers?

A. Yes. The sale will benefit customers by furthering the Commonwealth's goal of moving generation to the competitive sector. In addition, for WMECO, its share of the substantial proceeds from the sale will mitigate its Transition Costs. Thus, the sale will have a direct and significant benefit to WMECO's customers. The Schwennesen Testimony (Attachment 3 to this filing) and the Collin Testimony (Attachment 4 to this filing), describe the benefits to the customers of NEP and FG&E, respectively. Finally, a further benefit is the elimination of the risk of future costs and liabilities related to the operation of the units or decommissioning at the units (other than the limited contributions to decommissioning funds discussed above) to which customers conceivably would otherwise be exposed.

IV. EXEMPT WHOLESALE GENERATOR STATUS

Q. Please explain the findings that have been requested of the Department under Section 32 of Public Utility Holding Company Act ("PUHCA").

Untitled

A. The Petitioners have requested the Department make certain findings that are required by §32 of PUHCA in order for DNC to be able to obtain EWG status. DNC will be seeking to have FERC determine that the Millstone generating assets (i.e., Millstone Unit 2 and Unit 3) are "eligible facilities" pursuant to §32 of PUHCA. The Petitioners are thus seeking a specific determination by the Department that allowing the generation assets to become "eligible facilities" pursuant to §32 of the 1935 Act: (1) will benefit consumers; (2) is in the public interest; and (3) does not violate state law. As further described below, the sale is contingent upon obtaining EWG status.

EWG status is necessary in order to avoid compliance with the burdensome requirements applicable to public utility company affiliates of holding companies under PUHCA. EWG status is critical to Dominion and DNC, because it allows ownership and operation of Millstone without regulation as a public utility company under the 1935 Act. The EWG exemption to PUHCA was specifically created in 1992 to avoid subjecting competitive generation to the restrictions of the 1935 Act and to enhance the creation of a competitive generation market. Few, if any, entities would have been willing to bid for Millstone if EWG status had not been made a condition of the sale. Without the EWG condition, the Millstone assets would be virtually unmarketable, and, in any event, the purchase price realized by the Petitioners and the other participating joint owners would likely have been greatly reduced. EWG status is a closing condition and, as such, is crucial to obtaining the previously

Untitled

described benefits to consumers.

Q. When do the Petitioners and the other parties to the PSA wish to close the sale of Millstone?

A. The parties wish to close this transaction on or about April 1, 2001. In order to remain on this time schedule, the Petitioners request Department approval by December 31, 2000.

Q. Does this conclude your joint testimony?

A. Yes, it does.